No. 88-2109

FILED

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In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI,
AS PARENS PATRIAE,

Petitioners,

v.

UTILICORP UNITED INC.,

Respondent.

On Writ Of Certiorari To The United States
Court Of Appeals For The Tenth Circuit

BRIEF FOR RESPONDENT UTILICORP UNITED INC.

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QUESTION PRESENTED

Petitioners' "Questions Presented" violate Supreme Court Rule 21.1(a) by the presentation of argumentative and repetitious questions. The issue presented to this Court should be the question certified by the District Court for interlocutory appellate review and ruled by the United States Court of Appeals for the Tenth Circuit pursuant to 28 U.S.C. § 1292(b):

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

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STATUTE INVOLVED IN THE CASE

In their petition for a writ of certiorari, the States of Missouri and Kansas cited the Court to Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982). In their brief on the merits, petitioners also seek to rely substantively on portions of Title III of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. §§ 15c, 15d, and 15e. The States did not rely substantively on Sections 4c through 4e in the Courts below.

STATEMENT OF THE CASE

A. Background.

UtiliCorp United Inc. sells natural gas to industrial, commercial, and residential customers in 12 towns in western Missouri through its Missouri Public Service division ("MPS") and in Lawrence, Kansas, through its Kansas Public Service division ("KPS"). J.A. 5, Doc. No. 440 at 61.[1] During the time of the anticompetitive combination alleged in its Complaint, UtiliCorp purchased natural gas directly from Williams Natural Gas Company ("Pipeline"). *Id.* at 7.

Pipeline had purchased that natural gas from various suppliers, including Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("Exploration"), the Moxa Limited Partnership ("Moxa"), and the Wamsutter Limited Partnership ("Wamsutter"). *See id.* at 9, 12-13.

In September 1984, The Kansas Power and Light Company ("KPL") filed a Complaint in Missouri pursuant to Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982), against defendants Pipeline, Amoco, Cities Service, Exploration, Moxa, and Wamsutter. Doc. No. 2. UtiliCorp subsequently intervened and filed a substantially similar Complaint against the same defendants alleging, *inter alia*, that the defendants, acting in combination, artificially inflated and fixed the price of natural gas that was produced by them in Wyoming and

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[1] References to "Doc. No. ___" are to the list of relevant docket entries in the Joint Appendix.

sold in interstate commerce by Pipeline to UtiliCorp and other direct natural gas purchasers. Doc. Nos. 60, 378.[2] The utilities' case was transferred to Oklanoma and ultimately to Kansas.

UtiliCorp seeks to recover overcharge damages for all natural gas purchased directly from the defendants which it used in its own operations or resold to its residential, industrial, and commercial customers. *See* Doc. No. 440 at 13-14. UtiliCorp also seeks to recover from defendants the margin[3] it lost as a result of decreased sales of natural gas due to defendants' anticompetitive conduct. *Id.*

Defendants asserted as an affirmative defense to UtiliCorp's Complaint that UtiliCorp had passed on any illegal overcharges to its customers ("the pass-on defense"). *Id.* at 2-3 and n.1. Defendants claimed that UtiliCorp therefore lacked standing under Section 4 of the Clayton Act and had not been injured within the meaning of that statute. *Id.* at 3.

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[2] Although it is not included in the Joint Appendix, UtiliCorp's First Amended Complaint was filed on August 3, 1989. The latest amendments have no bearing on the issues before this Court.

[3] In their Brief, petitioners simplistically refer to the utilities' lost profit claims. *See, e.g.*, Petitioners' Brief at 14-15. In fact, the utilities' damage claims encompass both a rate of return element that was lost due to defendants' conduct and an amount representing the portion of the utilities' fixed costs which they were not able to recover because of defendants' conduct. The utilities' damage calculations are more complicated than the States' Brief would suggest.

Following the utilities' lead, the States of Kansas and Missouri filed Complaints under Section 4 of the Clayton Act against the same defendants in July of 1985 and August of 1986, respectively. J.A. 1. The States' allegations are virtually identical to those of the utilities. *Id.* The petitioners seek to recover overcharge damages on behalf of state agencies and municipalities[4] that purchased natural gas directly or indirectly from Pipeline and as *parens patriae* on behalf of indirect residential gas customers in their respective states. Doc. Nos. 345, 348.

The States do not – and cannot – assert claims on behalf of UtiliCorp's industrial and commercial natural gas customers in Kansas and Missouri. As a result, the States' *parens patriae* claims represent no more than 50 percent of the natural gas sold by the Pipeline in Missouri and Kansas. Exhibit A to Doc. No. 440 at 2, ¶ 4; Exhibit B to Doc. No. 440 at 2, ¶ 3. Acceptance of the States' *parens patriae* claims and the defendants' corresponding pass-on defenses would eliminate more than 50 percent of the antitrust damages asserted by the utilities in this case against the defendant producers and suppliers. *Id.*

B. Proceedings Below.

In December 1987, UtiliCorp filed a motion to strike or for partial summary judgment on those affirmative

[4] The States' claims on behalf of direct purchaser cities which distribute natural gas to their residents through a municipal utility are analogous to the claims of UtiliCorp. For example, the City of Springfield, Missouri, has claims for all overcharges, including those it passed along to residential, industrial, and commercial customers, in an amount exceeding UtiliCorp's overcharge damages. *See* Doc. No. 348.

defenses asserted by Amoco, Cities Service, and Pipeline which were based on the pass-on theory rejected in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968). Doc. No. 440. Shortly thereafter, KPL filed a similar motion. Doc. Nos. 448, 449.

Contrary to the States' representation at page 6 of Petitioners' Brief, neither UtiliCorp nor KPL asked for dismissal of the States' *parens patriae* claims – the motions were directed solely toward defendants' affirmative defenses. *See* Doc. No. 440. The private counsel hired to represent Missouri and Kansas insisted that the District Court also consider the dispute as a motion to dismiss the States' *parens Patriae* claims. *See* Doc. Nos. 474, 485.

The District Court, the Honorable Dale E. Saffels,[5] found on uncontested evidence that UtiliCorp and KPL did not resell natural gas pursuant to cost-plus contracts for fixed quantities. *In re Wyoming Tight Sands Antitrust Cases*, 695 F. Supp. 1109 (D. Kan. 1988), *aff'd*, 866 F.2d 1286 (10th Cir. 1989), *cert. granted sub nom. Kansas v. Kansas Power & Light Co*, 110 S. Ct. 833 (1990)(A34). Accordingly, it entered partial summary judgment prohibiting the defendants from asserting pass-on defenses to the antitrust claims of UtiliCorp and KPL. *Id.*

Following the suggestion of the States' counsel that issues of the States' *parens patriae* standing and injury also

[5] Prior to his appointment to the federal bench, Judge Saffels had extensive experience in utility regulation. He served as a member and then as Chairman of the Kansas Corporation Commission, which regulates Kansas utilities, from 1967 to 1975.

be resolved, the District Court dismissed the States' *parens patriae* claims pursuant to the holding of *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), prohibiting offensive use of pass-on theories. In so ruling, the District Court made no determination regarding the amount of illegal overcharges allegedly passed on by UtiliCorp to its customers. *Wyoming Tight Sands*, A33-34.

In neither the District Court nor in the Court of Appeals for the Tenth Circuit did counsel for the States contend that Section 4c of the Clayton Act created an independent cause of action for state attorneys general on behalf of indirect purchasers. *See* Doc. Nos. 474, 485. The District Court did not address that issue, which was briefed for the first time in this Court in petitioners' brief on the merits.

None of the defendants appealed from the District Court's entry of partial summary judgment prohibiting their use of pass-on defenses. On the States' motion, the District Court certified for interlocutory appeal the question of whether indirect residential purchasers of natural gas may join their own local distribution companies in asserting federal antitrust claims against the producers and an intermediary pipeline supplier of natural gas. Doc. Nos. 528, 541. The Court of Appeals for the Tenth Circuit granted the States' unopposed petition for permission to appeal. Doc. No. 555.

The Court of Appeals affirmed Judge Saffels' Order, concluding that the rulings and rationales underlying *Hanover Shoe* and *Illinois Brick* prohibit the needless and expensive complication of ongoing federal antitrust litigation which the States' *parens patriae* claims would

cause. *Wyoming Tight Sands*, A17. Although the Court below recognized that the States had not argued that Section 4c of the Clayton Act eliminates the *Illinois Brick* direct purchaser rule, it assumed that under Section 4c, citizens of a state must have standing in order for the state attorney general to sue in its *parens patriae* capacity. *Id.* at A7 n.1. The Court of Appeals implicitly concluded that the utilities' residential customers are indirect purchasers barred from recovery by *Illinois Brick*.

Petitioners' Statement of the Case ends with one misleading statement that demands correction: the suggestion that "the utilities will be entitled to recover *for their own benefit* all of the antitrust overcharges. . . ." Petitioners' Brief at 8 (emphasis added). The utilities have always acknowledged that recovery of overcharges will be passed back to the customers. *See, e.g.*, Doc. No. 440 at 17-18 ("UtiliCorp recognizes that its consumers will be the ultimate beneficiaries of much of the recovery extracted from defendants as damages.").

As Judge Saffels found, "[i]f the utilities prevail on their antitrust claim, their recovery will be passed on to the consumers either through a reduction in prices or through a rebate. This appears to be an eminently fair and efficient means of apportioning any damage award, much more so than through protracted litigation." *Wyoming Tight Sands*, A36. Despite this knowledge, the utilities have pursued this litigation vigorously, at no cost to the ratepayers, to protect their markets, recover their lost margins, and win a treble damage award.

SUMMARY OF THE ARGUMENT

This case presents a straightforward issue of antitrust policy: Should this Court continue to consolidate antitrust damage claims in the hands of an injured direct purchaser to reduce complexities and maximize the incentive to sue? Or, instead, should the Court cloud the clear rule of *Hanover Shoe* and *Illinois Brick* with a regulated utility exception created for the benefit of state attorneys general suing in their *parens patriae* capacity on behalf of some customers who ultimately paid some of the overcharges?

UtiliCorp is clearly an injured direct purchaser under Section 4c of the Clayton Act and this Court's precedents. As a direct purchaser of gas from an anticompetitive combination, UtiliCorp suffered more than $4 million in lost margin damages which were not "passed on" to its customers, and it paid more than $12 million in overcharges. While most of the overcharges were passed on to residential, commercial, and industrial customers, the States' claim that residential customers in Kansas and Missouri "bore *all* antitrust overcharges," Petitioners' Brief at 10 (emphasis added), is false.

In this case, the utilities are in the best position to maintain antitrust claims. They have ample incentive to pursue millions of dollars in damages and can also satisfy the concerns of the state public service commissions by passing through much of the recovery to their customers. Concentrating the claims in the utilities avoids complex battles over apportionment of damages and the disincentive of fragmenting the recovery among multiple levels of purchasers.

To the extent that the Court in *Illinois Brick* hypothesized an exception to the direct purchaser rule for fixed quantity, cost-plus contracts, that theoretical exception does not apply to this case because UtiliCorp never sold gas pursuant to fixed quantity contracts. The States' *parens patriae* claims do not "fit squarely within the 'cost-plus' exception," Petitioners' Brief at 8.

Petitioners' attempt to claim that Section 4c of the Clayton Act creates an independent cause of action cannot be considered by this Court because it was never raised below. Moreover, in *Illinois Brick* this Court rejected the notion that the Hart-Scott-Rodino Antitrust Improvements Act of 1976 created a new remedy for indirect purchasers represented by state attorneys general. Subsequent testimony by state attorneys general and comments by members of Congress confirm that this Court's interpretation was and is correct. On several occasions, Congress has refused to amend Section 4c to repeal or modify the *Illinois Brick* direct purchaser rule, thus demonstrating Congress' approval of the case and the rule it announced.

ARGUMENT

I. UTILICORP'S SECTION 4 CLAIMS ARE PROPER BECAUSE IT SUSTAINED ANTITRUST INJURIES INFLICTED BY THE DEFENDANTS.

More than 20 years ago, this Court identified the direct purchaser as the proper plaintiff to pursue damages resulting from antitrust violations under § 4 of the Clayton Act. *See Hanover Shoe*. The Court reached that

conclusion even though it recognized that the direct purchaser could have passed on all illegal overcharges to its customers. *Hanover Shoe*, 392 U.S. at 489-91 and n.8.

UtiliCorp is a direct purchaser of natural gas from the defendant combination. As a result of the defendants' anticompetitive conduct, UtiliCorp has sustained antitrust injury in excess of $4 million in lost margin damages. In addition, it paid more than $12 million of overcharges for natural gas from the defendants' combination.

Roughly half of that gas was resold to the residential customers the Attorneys General attempt to represent. *See* Exhibit A to Doc. No. 440 at 2, ¶ 4; Exhibit B to Doc. No. 440 at 2, ¶ 3. Most of the rest[6] was sold to industrial and commercial customers who are not represented in the *Wyoming Tight Sands* litigation. *Id.*

Even though UtiliCorp was ultimately reimbursed for most of the overcharges when its customers purchased the gas, under Section 4(a) of the Clayton Act UtiliCorp is the proper party to seek recovery for both the overcharges and the lost margin damages it suffered. *See Hanover Shoe*, 392 U.S. at 489.

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[6] UtiliCorp also uses small amounts of Pipeline gas for internal operations, principally for heating company facilities and to power turbine peaking units in MPS' electrical distribution network.

In 1977, this Court reaffirmed the policies and principles of *Hanover Shoe* in *Illinois Brick*. In that case, the Court refused to allow an indirect purchaser to claim antitrust injury. Once again, a direct purchaser's ability to pass on overcharges to its customers did not create injury and standing under federal antitrust laws on the part of the indirect purchasers who absorbed the overcharges.

This Court invited parties dissatisfied with that rule to seek legislative amendments to the Court's interpretation. *Illinois Brick*, 431 U.S. at 733-34 n.14. Congress has rejected every proposal to effect such changes.

Having failed in their efforts to overrule *Illinois Brick* legislatively, the state attorneys general are back before this Court, seeking to whittle away at the basic federal antitrust principle that direct purchasers suffer the antitrust injury. Yet in the thirteen years since *Illinois Brick* was decided, nothing has occurred to justify a judicial exception to the rule that direct purchasers who suffer some damage incur an injury to their business or property as contemplated in Section 4 of the Clayton Act.

In *ARC America*, this Court recently reaffirmed the direct purchaser rule, stating flatly that "[a]s construed in *Illinois Brick*, § 4 of the Clayton Act authorizes only direct purchasers to recover monopoly overcharges under federal law." *California v. ARC America Corp.*, 490 U.S. ___, 109 S. Ct. 1661, 1666, 104 L. Ed. 2d 86, 96 (1989). The policies underlying this rule support the Court of Appeals' judgment in this case.[7]

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[7] The States have cited a footnote from *ARC America* out of context in an attempt to carve greater territory for indirect

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II. FEDERAL ANTITRUST POLICY SUPPORTS CONCENTRATING DAMAGES IN THE HANDS OF THE DIRECT PURCHASER TO INCREASE HIS INCENTIVE TO ACT AS A PRIVATE ATTORNEY GENERAL.

The issue of antitrust policy before the Court is whether it remains wise to consolidate antitrust damage claims in the direct purchaser in order to maximize the incentive for private parties to sue. Effective enforcement of the antitrust laws depends on the vigor of private attorneys general in pursuing treble damage awards for their own profit. Deterrence is furthered more by concentrating a claim in the hands of a direct purchaser utility with a large damage claim and a profit motive than by splitting off parts of that claim to be handled by the overworked staffs of various state attorneys general.

The States search for an exception to the direct purchaser rule of *Hanover Shoe* and *Illinois Brick* based on an

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purchasers than permitted by *Hanover Shoe* or *Illinois Brick*. *See* Petitioners' Brief at 13. The Court's primary concern in footnote 6 to *ARC America* was not to diminish the injury or standing of direct purchasers such as UtiliCorp, but to ensure that "at least some party have sufficient incentive to bring suit." *ARC America*, 109 S. Ct. at 1666 n.6, 104 L. Ed. 2d at 96 n.6. For the reasons set forth below, that incentive properly belongs to the utilities who purchased directly from the anticompetitive combination.

Petitioners also inaccurately characterize *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982), as an "indirect purchaser" case. *See* Petitioners' Brief at 19-20. In *McCready*, this Court found that the plaintiff was essentially the direct purchaser. *Id.* 457 U.S. at 475.

expansive reading of hypothetical illustrations suggested in those opinions and on the Seventh Circuit's regulated utility exception posited in *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.)(en banc), *cert. denied*, 109 S. Ct. 543 (1988). This Court's hypothetical exception to the direct purchaser rule recognized that the direct purchaser could not be damaged if it passed on 100% of the illegal overcharges *and* was insulated from declining sales and profits by a fixed quantity cost plus contract. *Hanover Shoe*, 792 U.S. at 493; *Illinois Brick*, 431 U.S. at 736.

In this case, however, the States acknowledge that the utilities can recover from the defendants lost sales and profits due to the anticompetitive combination. *See* Petitioner's Brief at 14-15. Moreover, the States conceded in their Reply Brief in the Court of Appeals that the utilities could also recover that portion of the overcharge damages attributable to the industrial and commercial customers who are not otherwise represented in this suit – a sum totalling over $100 million for UtiliCorp and KPL. States' Reply Brief at 2.[8]

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[8] The Court may note some theoretical inconsistency in the States' position on the standing/antitrust injury of indirect residential customers versus indirect industrial and commercial customers. Under Section 4c(a)(1), of course, state attorneys general cannot represent business entities. While both elected officials are pleased to represent over one million residential customers in this case, neither wants to accept responsibility for a decision of this Court that could allow the defendants to keep over $100 million of overcharge damages attributable to the industrial and commercial customers who did not bring suit.

In *Illinois Brick*, this Court recognized that "the process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Illinois Brick*, 431 U.S. at 744-45. The Court further noted that "*Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses, and we adhere to the narrow scope of exemption indicated by our decision there." *Id.* at 745.

The Court below correctly applied the principles of *Hanover Shoe* and *Illinois Brick*. In particular, the Court stressed the need to avoid the addition of unnecessary complexity and expense to this case and to ensure the efficient enforcement of federal antitrust laws. *See Wyoming Tight Sands*, A9, *citing Illinois Brick*, 431 U.S. at 737, 745-48.

First, the Tenth Circuit noted that "[c]omplex issues of proof will grow geometrically if the States press their consumers' demands" (A10), due in part to the unresolved factual issue of how much illegal overcharge was passed on to the residential consumers of each utility. Contrary to the States' promise of simple damage apportionment, the Court below recognized that "[a]ny allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state . . . " *Id.* at A12. The Tenth Circuit also correctly observed that even a perfect pass-on of all overcharges would not eliminate the need to apportion the damages

sustained by UtiliCorp as a result of decreased demand caused by defendants' inflated prices. *Id.* at A14.

A. Complexity

Because this issue was raised toward the outset of the litigation, at the beginning of deposition discovery, the parties had only rough estimates of the amount of overcharge damages, elasticities of demand, and lost margin damages that would be claimed at trial. In fact, only within the last few months have plaintiffs' economic experts completed their calculations of damages.

The complexity of such economic analyses and the time such studies take confirms this Court's preference for the simple "direct purchaser rule" of *Hanover Shoe* and *Illinois Brick*. If preliminary issues of injury and standing turned on sorting out the classes of recovery in every case, those issues would often become a procedural roadblock that defendants would use as a way to stall the litigation from proceeding on the merits. *See Associated General Contractors, Inc. v. California State Council of Carpenters*, 459 U.S. 519, 544 (1983) (in *Hanover Shoe*, the Court "noted that any attempt to ascertain damages with such precision 'would often require additional long and complicated proceedings involving massive evidence and complicated theories.' "), *quoting Hanover Shoe*, 342 U.S. at 493.

Recognizing an exception to the direct purchaser rule in this case will also greatly complicate proof of damages and could well result in jury confusion. Both risks would reduce the incentive for pursuing antitrust claims.

All these factors demonstrate why this Court should decline to adopt Judge Posner's result-oriented opinion in *Panhandle Eastern*. Even if the Court approved of the Seventh Circuit's concept, the relatively simple facts in that case do not support wide application of a new exception and distinguish it from the more complicated situation in *Wyoming Tight Sands*.

The Court in *Panhandle Eastern* dealt with the customers of a single utility in a single state with a single set of rate regulations. This case involves numerous utilities operating in four states with multiple municipal and state regulatory schemes. *See Wyoming Tight Sands*, A13-14.

The trial of this case will be complicated enough without asking the jury to apportion damages among the various parties and classes of customers they claim to represent. For example, KPL claims lost margin on all of its sales; overcharge damages attributable to all its customers in Nebraska and Oklahoma; its "own use" overcharge damages; and overcharge damages attributable to its industrial and commercial customers in Kansas and Missouri.

The States each claim overcharge damages on behalf of their residential customers and their indirect purchaser governmental customers such as universities, county governments, school districts, prisons, libraries, fire districts, and municipal governments. In addition, the direct purchaser city utilities represented by the Attorneys General are entitled to claim damages for overcharges attributable to commercial and industrial customers. Direct purchaser Farmland Industries, Inc., also claims lost profits and overcharge damages.

By the time the trial reaches UtiliCorp's separate damage claims for its Kansas Public Service and Missouri Public Service divisions as well as its "own use" and lost margin claims, the jury may be inescapably confused.

In an effort to gloss over the complexities inherent in this case, the States have failed to explain the details of natural gas distribution in Missouri and Kansas. The sale of natural gas by UtiliCorp's KPS and MPS division does not lend itself to a simple calculation of the impact of illegal overcharges by the defendants.

In attempting to describe state natural gas regulation in Kansas by the Kansas Corporation Commission ("KCC") and in Missouri (by the Missouri Public Service Commission), the States would have this Court believe that all natural gas utilities operating in Kansas and Missouri were at all relevant times subject to state authority and resold natural gas pursuant to identical state-approved Purchased Gas Adjustment ("PGA") clauses. To the contrary, the municipal utilities set their own rates. KPS, as a "one city" utility, was not subject to KCC authority until 1987 and, during most of the relevant period, did not resell natural gas by way of a PGA mechanism.[9]

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[9] In Kansas, privately-owned public utilities situated and operated wholly or principally within one city for the exclusive benefit of that city are not subject to KCC authority and regulations. *See* K.S.A. § 66-104 (1985). In 1985, UtiliCorp acquired another utility which distributes natural gas to a few Kansas towns. For this reason, the KPS division of UtiliCorp lost its "one city" exception and had to seek a KCC certificate, which was approved in November 1987.

Because KPS was not subject to KCC authority during most of the relevant period, it did not resell natural gas pursuant to a PGA mechanism. During that period, KPS presented its requests for rate adjustments to the Lawrence City Council. UtiliCorp's Motion for Partial Summary Judgment (Doc. No. 440; J.A. 5), *citing* Exhibit B, Affidavit of KPS President William A. Salome, III, at 2, ¶ 5. No formula comparable to MPS' PGA clause was used to determine or evaluate rate modifications sought by KPS. *Id.*, *citing* Salome Affidavit at 2, ¶ 6.

Although MPS is subject to Missouri Public Service Commission authority, some of the towns in which it distributes natural gas are served by another pipeline not involved in the defendant combination. This factor also complicates the damage analysis because rate cases normally covered both of the MPS gas systems.

For these reasons, UtiliCorp denies the States' unsupported contention in footnote 7 on page 13 of their Brief that the regulatory mechanism set forth in the testimony of KPL employee David S. Black "operates the same way with respect to respondent UtiliCorp." UtiliCorp's complex gas distribution systems for KPS and MPS demonstrate the wisdom of the rationales *Hanover Shoe* and *Illinois Brick*.

If the States' argument is accepted, proving or disproving plaintiffs' damages at trial will require all parties to introduce complex evidence tracking each unit of gas sold from the wellhead, through the pipeline, to the utilities, and ultimately to the burner tip. There is nothing simple or uncomplicated about the process. Asking lay

jurors to interpret damage claims based on such complicated, regulated pricing systems invites confusion and error which would be reduced greatly if UtiliCorp proves its claims directly.

B. Avoiding Multiple Liability

The risk of multiple liability which concerned the Court in *Illinois Brick*, 431 U.S. at 730, is eliminated by the Tenth Circuit's affirmance of the District Court's Order. As long as this Court maintains the direct purchaser rule of *Hanover Shoe* and *Illinois Brick*, there is no risk of multiple recovery under the federal antitrust laws.

C. Incentive

UtiliCorp claims at least $12 million in overcharge damages and $4 million in lost margin. When damages are trebled, UtiliCorp stands to recover $48 million.

Together, UtiliCorp and KPL account for roughly 75% of the overcharges and claim more than $250 million in actual damages.[10] These utilities have used their ample

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[10] Petitioners' Brief at 17 misleadingly claims that 48 Missouri and Kansas utilities failed to join this suit. All the Missouri utilities served by the Pipeline are parties to this suit: UtiliCorp, KPL, and four municipal utilities represented by the Missouri Attorney General.

In Kansas, 37 small municipal uitilities are supplied by the Pipeline. Presumably, they are all represented by the Kansas Attorney General.

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resources to mount a vigorous prosecution of the defendants' anticompetitive conduct.

The States ignore the fact that it is the utilities who, in the first instance, bear the financial responsibility for the natural gas purchased. UtiliCorp must pay for the natural gas purchased from the Pipeline, regardless of whether it ultimately recoups that amount from its customers. So long as UtiliCorp is liable as a direct purchaser for the costs of the natural gas it purchases for resale, it has more than ample incentive to monitor defendants' actions.

Moreover, UtiliCorp has an incentive to protect its markets. Industrial customers who transport gas or any customer who conserves or uses alternative fuels to reduce his purchases represents a potentially permanent loss of UtiliCorp's market. Customers who believe that the utility is looking out for their interests are more likely to defer seeking permanent alternative sources of energy.

The utilities' demonstrated commitment to the interests of their customers and the lure of treble damages has

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The only two significant Kansas utilities not represented in this lawsuit are Peoples Natural Gas and Union Gas. Those utilities have protected their customers by intervening in a proceeding pending before the Federal Energy Regulatory Commission which also challenges defendants' conduct. *See Midwest Gas Users Ass'n v. FERC*, 833 F.2d 341 (D.C. Cir. 1987).

Only a handful of tiny Kansas investor-owned utilities supplied by the Pipeline have failed to pursue either an antitrust claim or a FERC claim arising out of defendants' anticompetitive combination. Those companies' aggregate purchases total less than one percent of Pipeline's sales.

caused them to advance millions of dollars in legal fees and expenses to pursue this litigation. This hard-fought case has proceeded even though the utilities recognize that their customers will be the ultimate beneficiaries of most of the overcharge portion of any award or settlement. Nevertheless, the States continue to argue that the utilities lack incentive to sue because they passed on the overcharges. Petitioners' Brief at 18-19.

The Court of Appeals for the Tenth Circuit concluded that permitting the States to pursue their claims in this case would imperil vigorous enforcement of the antitrust laws by taking away the incentive to prosecute alleged antitrust violators from the direct purchaser – who is closer to the violator and presumably has better access to information about wrongful acts – and transferring the cost of policing and enforcing federal antitrust laws to the states. *Wyoming Tight Sands*, A14.

Rejecting the States' assertions, the Court of Appeals concluded that state attorneys general are *not* the most reliable parties to pursue overcharge damages on these facts.[11] The Court below recognized that the States'

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[11] The States' purported concern about the potential impact of the statute of limitations on UtiliCorp's antitrust claims is not well founded. A critical event which all plaintiffs describe in their Complaints was the defendants' certain amendments of gas purchase contracts on March 17, 1981. *See* Doc. No. 440 at 11-12. Both the State of Kansas and the State of Missouri filed suit more than four years after the signing of the 1981 amendments. J.A. 1. Kansas, Missouri, and UtiliCorp must all rely on arguments of fraudulent concealment by the defendants in order to avoid the four year statute of limitations for federal antitrust claims.

belated willingness to join in this particular action provides no assurance whatsoever of aggressive antitrust enforcement in other cases. *Id.* at A10.

Judge Posner contends that indirect purchaser consumers benefit from concentrating recovery in the hands of direct purchaser middlemen. *See* R. Posner, *Economic Analysis of Law* 294-95 (3rd ed. 1986). He also questions whether state attorneys general are truly vigorous advocates on whom society can rely to enforce the antitrust laws:

> Given the political character of *parens patriae* enforcement, it is doubtful that it can be relied upon as an adequate antitrust deterrent. There may well be a tendency under *parens patriae* for state attorneys general to bring headline-grabbing, scapegoat-seeking suits against politically unpopular corporations, with little regard for the intrinsic antitrust merit of the suit and with little effort to press the suit to a successful conclusion. By the time the case is ready for trial, the state attorney general's office may be occupied by a new politician with little interest in carrying out the projects of his predecessor.

W. Landes & R. Posner, *Should Indirect Purchasers Have Standing to Sue Under the Antitrust Laws? An Economic Analysis of the Rule of Illinois Brick*, 46 U. Chi. L. Rev. 602, 613 (1979).[12]

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[12] *See also* Minority Report on P.L. 94-435, H.R. Rep. No. 94-499, 94th Cong., 2d Sess. 24-25, *reprinted in* 1976 U.S. Code Cong. & Ad. News 3, 2593. ("We believe that politics and antitrust will not make a happy marriage. The temptations for the politically ambitious to ride into the public eye as its champion against "fat cat" antitrust violators by filing lawsuits to the sound of political trumpets may be too great. Since antitrust cases take years to complete, the politically ambitious

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In addition, because "[t]he antitrust units of the states are generally understaffed and subject to budgetary constraints," state attorneys general are often unable to follow through with the trial of antitrust cases. T. Wilson, *Defending An Antitrust Action Brought By a State AG*, 1 A.B.A. Antitrust 10, 14 (1987).[13]

Neither Missouri nor Kansas pursued this case until KPL completed the thorough investigation necessary to evaluate and file a complex antitrust suit. KPL actually encouraged the Attorneys General of Missouri and Kansas to enter the case on behalf of municipal utilities served by the Pipeline. This litigation proves that federal antitrust enforcement responsibility should not be splintered among direct purchasers and state attorneys general bringing *parens patriae* claims on behalf of indirect purchaser consumers.

The possibility that state public utility commissions may threaten to take away all incentives from the utilities by passing through all damages they recover to the

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attorney general need not fear the embarrassment of a string of losses. In any event, many of the cases will have been undoubtedly settled because of their adverse publicity and their nuisance value.").

[13] Footnote 9 on page 19 of the Amici Brief of the Forty-Six States underscores this point. Of the seven cases cited as support for the "powerful and effective weapon" of *parens patriae* suits, all were settled.

The states claim great expertise in enforcing the antitrust laws, Forty-Six States' Amici Brief at 21, but neglect to mention that in this case both Kansas and Missouri have hired private attorneys to prosecute their claims.

consumers is largely within the states' control. If the States fear that these utilities lack a sufficient incentive to pursue claims against antitrust violators, then the answer lies in rewarding utilities for their initiative by allowing their stockholders to keep the treble damages portion of the recovery. Alternatively, the regulatory commissions could punish utilities who refuse to pursue meritorious antitrust suits by refusing to allow them to pass on overcharges or by forcing them to turn some portion of the overcharges to the customers.

Petitioners cannot be permitted to strip the utilities of their motivation to sue and then to contend that the disincentive created by the States justifies *parens patriae* claims on behalf of indirect residential purchasers. Moreover, federal antitrust policy should not be held hostage to the relationship between a state utility commission and either the utilities it regulates or the state's attorney general.

The goals of the antitrust laws in recouping illegal overcharges and punishing wrongdoers will best be served by allowing UtiliCorp, KPL, and the municipal utilities to pursue their direct purchaser antitrust claims against the defendants.

III. NO EXCEPTION TO THE DIRECT PURCHASER RULE SHOULD BE RECOGNIZED IN THIS CASE.

In an effort to keep their *parens patriae* claims alive, petitioners seek to wring from *Illinois Brick* an exception based on the regulated nature of the natural gas industry. The short answer to their argument is that no exception is

needed in this case to serve the policies of the antitrust laws.

Although a "cost-plus" exception to the "no pass-on" rule might apply when the direct purchaser "has not been damaged," *Hanover Shoe*, 392 U.S. at 494, UtiliCorp has alleged damages which this Court has concentrated solely in the hands of direct purchasers. This Court specifically recognized in *Hanover Shoe* that direct purchasers would incur recoverable damages if total sales declined as a result of illegal overcharges. *Id.* at 493.

In *Illinois Brick*, the Court explained that the cost-plus exception to the rule barring offensive and defensive use of pass-on theories applies only if "the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." *Illinois Brick*, 431 U.S. at 736. The hypothetical cost-plus exception mentioned in *Illinois Brick* does not apply in this case because UtiliCorp's customers do not purchase natural gas under preexisting, fixed quantity contracts. *See Wyoming Tight Sands*, A34, *aff'd*, A12.

Other courts have also recognized the requirement of a fixed quantity contract between direct and indirect purchasers before the pass-on defense can be asserted. *See Jewish Hospital Ass'n v. Stewart Mechanical Enterprises, Inc.*, 628 F.2d 971, 976 (6th Cir. 1980), *cert. denied*, 450 U.S. 966 (1981); *Mid-West Paper Products Co. v. Continental Group, Inc.*, 596 F.2d 573, 577 n.9 (3rd Cir. 1979); *Eastern Air Lines, Inc. v. Atlantic Richfield Co.*, 609 F.2d 497, 498, 499 (Emer. Ct. App. 1979); *Lefrack v. Arabian American Oil Co.*, 487 F. Supp. 808, 818-20, 822-23 (E.D.N.Y. 1980).

The rationale behind the cost-plus exception to *Illinois Brick* focuses on whether a direct purchaser can require its customers to buy a fixed quantity, thereby permitting the direct purchaser to pass through an illegal price increase without suffering ill effects. Where the indirect customers are obligated to buy a fixed quantity of product regardless of price increases, the distributor is completely shielded from damage resulting from the illegal overcharge. Only with cost-plus contracts for fixed quantities can courts be sure that the direct purchaser is not damaged.

That rationale does not apply in this case. UtiliCorp's customers purchase only that amount of natural gas which satisfies their individual needs and budgets. As testimony in the case confirms, consumers decrease their purchases in response to higher prices.

The Court should reject the reasoning of the Seventh Circuit in *Panhandle Eastern* applying a cost-plus exception to the direct purchaser rule in the absence of a fixed quantity purchase. Regulated public utility markets do not justify different ground rules for recognition of a cost-plus exception. *See Illinois Brick*, 431 U.S. at 743-44. Because increased natural gas costs have affected both UtiliCorp's volume of resold gas and its profits in accordance with the market forces of supply and demand, the creation of a regulatory equivalent to the cost-plus exception based on public utility regulation would be a mistake that would weaken enforcement of the antitrust laws.[14]

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[14] If the Court were inclined to create a public utility pass-on exception to the direct purchaser rule, UtiliCorp's recovery

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IV. THE STATES' BELATED RELIANCE ON SECTION 4c OF THE CLAYTON ACT DOES NOT BAR UTILICORP'S SECTION 4 CLAIMS.

A. The States' Section 4c Argument Violates Supreme Court Rule 24.1(a).

In their brief on the merits, petitioners urge the Court to reverse the Tenth Circuit's judgment for the "separate reason" that Section 4c of the Clayton Act authorizes *parens patriae* actions on behalf of indirect purchasers. Until this Brief, the States have never argued that Section 4c provides an alternative substantive reason for avoiding the bar of *Illinois Brick*.

The States' failure to raise Section 4c in their briefs filed in the District Court, in their Tenth Circuit brief and oral argument, and in their petition for a writ of

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of overcharge damages attributable to its commercial and industrial customers should remain unaffected by the Seventh Circuit's opinion in *Panhandle Eastern*. Judge Posner recognized that the industrial market for natural gas differs substantially from the residential customer market. *Panhandle Eastern*, A58.

Because industrial customers possess fuel-switching capabilities, Judge Posner argued that public utilities do not exercise the degree of monopoly power over customers which served as the rationale for the Seventh Circuit's "regulatory" equivalent to a possible cost-plus exception. Given a different factual record, the Court was not required to sacrifice the overcharges passed on to the utility's commercial and industrial customers – in stark contrast to the elimination of more than 50% of the damages claimed by the utilities in this case which would occur if the States' pass-on theories were permitted.

certiorari[15] forecloses consideration of that question as part of petitioners' brief on the merits. *See* Supreme Court Rule 24.1(a). *See also United States v. Lovasco*, 431 U.S. 783, 788 n.7 (1977); *Neely v. Martin K. Eby Construction Co.*, 386 U.S. 317, 330 (1967); *Duignan v. United States*, 274 U.S. 195, 200 (1927).

In their petition, the States sought a writ of certiorari to resolve one "critical question":

> Do indirect purchasers, who by regulatory mandate pay *all* of the illegal antitrust overcharges, fall within an exception to the general rule that only direct purchasers of a product have standing to seek antitrust damages from antitrust violators. The Seventh Circuit says "yes"; the Tenth Circuit says "no".

Petition at 8 (emphasis in original).

Those "yes" or "no" answers were to the question of whether a regulatory cost-plus exception to the Clayton Act may exist under *Hanover Shoe* and *Illinois Brick*. Neither the Seventh Circuit in *Panhandle Eastern* nor the Tenth Circuit in this case was presented with a Section 4c argument, and neither of the petitions for writs of certiorari addressed that issue.

Throughout the briefing and argument in the Courts below, the States have focused exclusively on the proposed cost-plus exception to *Illinois Brick* to the exclusion of any consideration of Section 4c of the Clayton Act. Petitioners' effort to divert the Court's attention to an issue not raised in the District Court or in the Tenth Circuit is improper under Supreme Court Rule 24.1(a).

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[15] In their petition, the States did not even cite Section 4c of the Clayton Act as a "statute involved in the case."

B. Section 4c Of The Clayton Act Does Not Bar UtiliCorp's Section 4 Claims.

Even if the Court were to consider petitioners' Section 4c argument on the merits, *parens patriae* causes of action do not bar UtiliCorp's claims under Section 4 of the Clayton Act. The *parens patriae* mechanism creates nothing more than "a new procedural device" to enforce existing rights of recovery under Section 4. *Illinois Brick*, 431 U.S. at 733-34 n.14. *See also In re Coordinated Pretrial Proceedings in Petroleum Products Antitrust Litigation*, 691 F.2d 1335, 1340 (9th Cir. 1982), *cert. denied sub nom. California v. Standard Oil Co.*, 464 U.S. 1068 (1984); *State of New York v. Dairylea Co-op, Inc.*, 570 F. Supp. 1213, 1215 (S.D.N.Y. 1983).

Congress' overriding purpose in enacting Section 4c was to provide state attorneys general with the power to enforce consumers' *existing* rights of recovery under Section 4.[16] In accordance with this intent, Congress included a notice provision in Section 4c for persons on whose behalf a *parens patriae* action is brought so that they could opt out of the case.[17] There would have been no reason

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[16] Taking half a sentence from a 1982 opinion out of context, petitioners erroneously assert that this Court has concluded that indirect purchaser suits are allowed under the Hart-Scott-Rodino Act because an indirect purchaser remedy "already existed." Petitioners' Brief at 29 n.19, *quoting Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 378 (1982). Instead of addressing *parens patriae* claims under Section 4c, *Merrill Lynch* arose out of private party claims under the Commodity Exchange Act.

[17] In this case, the States of Missouri and Kansas have never followed the requirements of 15 U.S.C. § 15c(b)(2) by providing a notice to consumers of their right to opt out.

for Congress to provide an "opt out" method for claims for which consumers had no cause of action. Moreover, if Congress had intended to give state attorneys general independent standing under federal antitrust laws, it would not have limited *parens patriae* claims to recovery only on behalf of those individuals who declined to opt out of the antitrust suit.

The States rely on the language and the legislative history of the Hart-Scott-Rodino Act to support their misinterpretation of Section 4c. Neither the Act itself nor the debates which preceded its passage support petitioners' statement that "[t]he Act cannot sensibly be read as authorizing *parens patriae* actions only on behalf of direct purchasers." Petitioners' Brief at 24.

When the Act was passed in 1976, this Court had not addressed the question of whether *Hanover Shoe's* rejection of the pass-on defense would be applied symmetrically to bar the claims of indirect purchasers. This Court resolved that ambiguity in 1977 in *Illinois Brick*, explicitly considering and rejecting the notion that Congress had intended for indirect purchasers to sue under Section 4c, but not under Section 4:

> Congress made clear . . . that this legislation did not alter the definition of which overcharged persons were injured within the meaning of § 4. * * * Representative Rodino himself acknowledged . . . that this legislation did not create a right of recovery for consumers where one did not already exist. * * * [W]e think the construction of § 4 adopted in [*Hanover Shoe*] cannot be applied for the exclusive benefit of plaintiffs. Should Congress disagree with this result, it may, of course, amend the section to change it. But it has not done so in the recent *parens patriae* legislation.

Illinois Brick, 431 U.S. at 733-34 n.14 (1977).[18]

In the thirteen years since *Illinois Brick*, Congress has repeatedly refused to amend Section 4c to overrule that opinion. Several state attorneys general have testified that legislative change is necessary because Section 4c does not create new remedies under the Clayton Act for *parens patriae* claims and *Illinois Brick* bars their *parens patriae* claims on behalf of indirect purchasers. *See Fair and Effective Enforcement of the Antitrust Laws, S. 1874: Hearings on S. 1874 before the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee*, 95th Cong., 1st Sess. 124 (1977) (Prepared statement of the California Attorney General) ("*Illinois Brick* . . . has virtually destroyed the right of indirect purchasers to recover damages under federal antitrust laws and has thereby seriously crippled the power of the States to enforce the antitrust laws pursuant to the recently enacted *parens patriae* legislation."); *id.*, 95th Cong., 2d Sess. at 109 (1978) (statement of the Arizona Attorney General). *See also Effective Enforcement of the Antitrust Laws, H.R. 8359: Hearings on H.R. 8359 Before the Subcommittee on Antitrust and Monopoly of the House Judiciary Committee*, 95th Cong., 1st

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[18] In footnote 14 to *Illinois Brick*, the Court cited to a brief filed by 47 States as amici curiae. In that brief, the states argued that *all* indirect purchasers should be permitted to maintain antitrust claims. They lost. In handing the states that defeat, this Court anticipated – and rejected – their argument in this case that liability standards of Section 4 differ from those of Section 4c.

Sess. 476 (1977) (letter from Washington's Attorney General Slade Gordon).

In lobbying Congress to amend Section 4c to allow for suits on behalf of indirect purchasers, state attorneys general have relied principally on an argument that, in the wake of *Illinois Brick*, the federal *parens patriae* statute does not permit them to use Section 4c to represent consumers who could not assert individual claims. They believed that *Illinois Brick* precludes them from representing indirect purchaser consumers.

In an unsuccessful attempt to respond to the states' concerns, the Senate Judiciary Committee recommended a remedial bill with these comments:

> [T]he majority opinion in *Illinois Brick* has emasculated *parens patriae*. [It] permits no other conclusion. If most consumers are indirect purchasers, and indirect purchasers are barred from suit, and the *parens patriae* provisions merely create "a new procedural device • • • to enforce existing rights," it follows by tautology that the *parens patriae* rights of State attorneys general are no greater than the underlying rights of consumers. • • • *The State attorneys general have uniformly reached that conclusion.*

S. Rep. No. 239, 96th Cong., 1st Sess. 25-26 (1979) (emphasis added). *See also* 129 Cong. Rec. H1549 (daily ed. March 22, 1983) (remarks of Representative Peter W. Rodino) (hereinafter cited as "129 Cong. Rec. H1549").[19] Congress'

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[19] The States contend that in Section 4c, "Congress intended to authorize state attorneys general to sue as *parens patriae* on behalf of indirect purchaser consumers," Petitioner's Brief

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refusal to amend the Clayton Act to reverse *Illinois Brick's* impact on Section 4c claims suggests that Congress is satisfied with *Illinois Brick* and does not desire to amend Section 4c to authorize *parens patriae* actions on behalf of indirect purchasers.

Finally, the States' reliance on the language of Section 4c is misplaced. The Act provides, in relevant part:

> . . . the court shall exclude from the amount of monetary relief awarded in such [*parens patriae*] action any amount of monetary relief (A) which duplicates amounts which have been awarded for the same injury, or (B) which is properly allocable to . . . (ii) any business entity.

Section 4c(a)(1) of the Clayton Act, 15 U.S.C. § 15c(a)(1) (1982). As a direct purchasing business entity, UtiliCorp stands first in line to recover overcharge damages under Section 4 of the Clayton Act.

Under both Sections 4 and 4c of the Clayton Act, UtiliCorp is the proper party to recover overcharge damages resulting from the defendants' anticompetitive conduct. Consumers are ultimately protected by the rule of *Illinois Brick* because the goals of avoiding complexity and duplication of damages and of vigorous enforcement

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at 26, citing Representative Rodino's remarks in the 1976 debates. Even if this Court had not already rejected that contention in footnote 14 of *Illinois Brick*, Representative Rodino's later statements in the 1983 debates on his proposed amendments to Section 4c demonstrate his agreement that *"Illinois Brick* negated this authority of State attorneys general" to sue on behalf of indirect purchasers. 129 Cong. Rec. H1549.

of the antitrust laws are best served when antitrust claims are asserted by direct purchasers.

CONCLUSION

The decision of the Court of Appeals should be affirmed.

Respectfully submitted,

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